State of North Carolina
Office of the State Controller

DAVID T. MCCOY
STATE CONTROLLER

September 21, 2011

MEMORANDUM

TO: Chief Fiscal Officers/Vice Chancellors

FROM: David T. McCoy David T. McCoy

SUBJECT: IRS Notice 2011-72, *Tax Treatment of Employer Provided Cell Phones* and IRS, *Memorandum For All Field Agents*, dated September 14, 2011

IRS Notice 2011-72, *Tax Treatment of Employer Provided Cell Phones*
The *Small Business Jobs Act of 2010* removed mobile communication devices (cell phones) from the definition of "listed Property". "Listed Property" is defined in IRC 280F(d)(4) and includes such items as computers, automobiles, cell phones, etc. IRC 274(d)(4) provides that no deduction shall be allowed with respect to any "listed property", unless the taxpayer substantiates by adequate records or by sufficient evidence corroborating the taxpayer's own statement: (a) the amount of such expense, (b) the use of the property, (c) the business purpose of the expense, and (d) the business relationship to the taxpayer of persons using the property.

By excluding cell phones from the definition of "listed property", cell phones now fall under the rules of "*working condition fringes*". IRC 132(d) provides that "*working condition fringe*" means any property or services provided to an employee of the employer to the extent that, if the employee paid for the property or services, such payment would be allowable as a deduction under IRC 162 or 167. For an expense to be allowable under IRC 162, it must be an "ordinary and necessary" business expense.

IRC 132(a)(4) provides that gross income does not include any fringe benefit which qualifies as a *de minimis fringe.* IRC 132(e) defines a *de minimis fringe* as any property or service the value of which is so small as to make accounting for it unreasonable or administratively impracticable.

Please Note, IRS Notice 2011-72 does not address the treatment of reimbursements received by employees from employers for the business use of an employee's personal cell phone.

IRS, *Memorandum For All Field Agents*, dated September 14, 2011
On September 14, 2011, the IRS issued a Field Memorandum concerning "Interim Guidance on Reimbursement of Employee Personal Cell Phone Usage in light of Notice 2011-72". This memorandum is to provide guidance to IRS examiners regarding employers that reimburse their employees for the business use of an employee's personal cell phone.

This IRS Field Memorandum states, "In cases where employers, for substantial noncompensatory business reasons, require employees to maintain and use their personal cell phones for business purposes and reimburse the employees for the business use of their personal cell phones, examiners should analyze reimbursements of employees' cell phone expenses in a manner that is similar to the approach described in Notice 2011-72." Furthermore, "the employee must maintain the type of cell phone coverage that is reasonably related to the needs of the employer's business, and the reimbursement must be reasonably calculated so as not to exceed expenses the employee actually incurred in maintaining the cell phone."

OSBM, *Budget Manual, Section 5.11 Mobile Communication Devices*

The OSBM, *Budget Manual, Section 5.11 Mobile Communication Devices* allows State agencies and institutions with a written cell phone policy to assign a state-owned cell phone to an employee, or to reimburse employees for the business use of an employee owned cell phone in certain circumstances.

Cell Phones Provided by State Agencies and Institutions

State agencies and institutions can provide cell phones to employees if the purpose is primarily for noncompensatory business reasons. The value of the ***business use*** ***of an State-provided cell phone is excludible from employee's income as a working condition fringe*** to the extent that, if the employee paid for the use of the cell phone themselves, such payment would be deductible to them under IRC 162. An employer is considered to have provide an employee with a cell phone primarily for noncompensatory business purposes if there are substantial reasons related to the employer's business, other than providing additional compensation to the employee. The ***personal use*** ***of the State provided cell phone should generally be excluded from the income of the employee as a de minimis fringe benefit***, providing the above conditions of *de minimis* use apply .

Reimbursement of Employee Owned Cell Phones by State Agencies and Institutions

Based on guidance provided in the IRS Field Memorandum of September 14, 2011, it now appears the IRS intends to treat employer reimbursement of employee owned cell phone expense in a manner similar to the treatment of employer provided cell phones. Thus, when a State agency/institution requires employees to maintain and use their personal cell phones for State business purposes and reimburses the employees for the business use, there should not be income to the employee provided the cell phone coverage is reasonably related to the needs of the agency/institution, and the reimbursement is reasonably calculated so as not to exceed expenses the employee actually incurred to maintain the cell phone. Also, the reimbursement for the business use must not be a substitute for a portion of the employee's regular wage.

In Summary

Agencies/Institutions providing cell phones to employees under the OSBM policy set forth in Section 5.11 of the *Budget Manual* should not be including the value of the personal use in the employee's wage. If the value of the personal use has been included in 2011 wage, it should be backed out prior to year-end.

Agencies/Institutions reimbursing employees for the use of employee owned cell phones may be able to exclude the value of the reimbursement from the employee's income providing the standards for exclusion set forth in the IRS Memorandum of September 14, 2011 are met. A copy of this Memorandum is attached for your review. This exclusion should be retroactive for reimbursements made in 2011.

Thank you for your attention to the above. Should you have questions, please call Randy Thomas at (919) 981-5488.

DTM/rt

Attachment:

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
Washington, D.C. 20224

September 14, 2011

Control Number: SBSE-04-0911-083
Expiration Date: September 19, 2012
Impacted IRM(s): 4.23.5

MEMORANDUM FOR ALL FIELD EXAMINATION OPERATIONS

FROM: Shenita Hicks /s/ Shenita Hicks
Director, Examination, SB/SE

John Imhoff /s/ John Imhoff
Director, Specialty Programs, SB/SE

David Horton /s/ David Horton
Director, Field Specialists, LB&I

Clifford J. Gannett /s/ Clifford J. Gannett
Acting Director, Government Entities, TE/GE

SUBJECT: Interim Guidance on Reimbursement of Employee Personal Cell Phone Usage in light of Notice 2011-72

The purpose of this memorandum is to provide audit guidance to examiners regarding employers that reimburse their employees for the business use of an employee's personal cell phone. This document is not intended to be a technical position, but to provide guidance to examiners who encounter this issue.

Notice 2011-72 addresses the tax treatment of employer-provided cell phones for noncompensatory purposes. The Notice provides that, for tax years after December 31, 2009, the IRS will treat the employee's use of employer-provided cell phones for reasons related to the employer's trade or business as *a working condition fringe benefit, the value of which is excludable from the employee's income.* However, the cell phone must be issued primarily for noncompensatory business reasons. For purposes of determining whether the working condition fringe benefit provision in § 132(d) applies, the substantiation requirements that must be satisfied by the employee for an allowable deduction under § 162 are deemed to be satisfied. Additionally, *any personal use of the employer-provided cell phone will be treated as a de minimis fringe benefit, excludable from the employee's gross income* under § 132(e) of the Code.

Notice 2011-72 does not address the treatment of reimbursements received by employees from employers for the business use of an employee's personal cell phone.

In cases where employers, for substantial noncompensatory business reasons, require employees to maintain and use their personal cell phones for business purposes and reimburse the employees for the business use of their personal cell phones, examiners should analyze reimbursements of employees' cell phone expenses in a manner that is similar to the approach described in Notice 2011-72. Specifically, in cases where employers have substantial business reasons, other than providing compensation to the employees, for requiring the employees' use of personal cell phones in connection with the employer's trade or business and reimbursing them for their use, examiners should not necessarily assert that the employer's reimbursement of expenses incurred by employees after December 31, 2009, results in additional income or wages to the employee. However, the employee must maintain the type of cell phone coverage that is reasonably related to the needs of the employer's business, and the reimbursement must be reasonably calculated so as not to exceed expenses the employee actually incurred in maintaining the cell phone. Additionally, the reimbursement for business use of the employee's personal cell phone must not be a substitute for a portion of the employee's regular wages. Arrangements that replace a portion of an employee's previous wages with a reimbursement for business use of the employee's personal cell phone and arrangements that allow for the reimbursement of unusual or excessive expenses should be examined more closely.

- Examples of substantial noncompensatory business reasons for requiring employees to maintain personal cell phones and reimbursing them for their use include: (1) the employer's need to contact the employee at all times for work-related emergencies; and (2) the employer's requirement that the employee be available to speak with clients at times when the employee is away from the office or at times outside the employee's normal work schedule (i.e., clients are in different time zones).

- An example of a reimbursement arrangement that does not result in additional income or wages is as follows: an employer has a substantial noncompensatory business reason for requiring the employee to maintain a personal cell phone to facilitate communication with the employer's clients during hours outside the employee's normal tour of duty in the office and reimbursing the employee for the use of the phone. The employee uses the cell phone for both business purposes and personal purposes and the employee's basic coverage plan charges a flat-rate per month for a certain number of minutes for domestic calls. The employer reimburses the employee for the monthly basic plan expense to enable the employee to maintain contact with business clients throughout the United States after hours.

- Examples of reimbursement arrangements that may be in excess of the expenses reasonably related to the needs of the employer's business and should be examined more closely include: (1) reimbursement for international or satellite cell phone coverage to a service technician whose business clients and other business contacts are all in the local geographic area where the technician works; or (2) a pattern of reimbursements that deviates significantly from a normal course of cell phone use in the employer's business (i.e., an employee received reimbursements for cell phone use of $100/quarter in quarters 1 through 3, but receives a reimbursement of $500 in quarter 4).

If you have any questions regarding these guidelines, you may contact Laird MacMillan, Senior Program Analyst.

cc: www.IRS.gov